



CORPORATE SOCIAL RESPONSIBILITY OF MULTINATIONAL CORPORATIONS

To what extent should multinational corporations contribute to improving social conditions in the economies in which they operate? Many multinational corporations operate in countries characterized by extreme poverty and inequality, inadequate or dysfunctional institutions, and undemocratic political systems. At the same time, multinational corporations are in a powerful position to promote change in developing countries, individually and/or collectively.

The question of corporate responsibility in poor and undemocratic countries, has been addressed by a CMI strategic institute programme (SIP) entitled "Business ethics for multinational corporations in developing countries". The programme, which has run from 2004 to 2006, has resulted in several international publications, and garnered significant media attention. This brief relates the major results of the programme.

THREE PERSPECTIVES ON BUSINESS ETHICS

The programme distinguishes between three different perspectives on business ethics:

- The *normative perspective* asks what corporations ought to do, what responsibilities do corporations have and to whom
- The *instrumental perspective* studies what responsibilities are profitable and in the interest of firms to pursue, and how firms can be given incentives to fulfil their other responsibilities
- The *descriptive perspective* asks what firms actually do in the area of business ethics

The programme has obtained important results for all three perspectives, which are highlighted in turn below.



WHAT ARE THE RESPONSIBILITIES OF CORPORATIONS?

Nobel Prize laureate Milton Friedman is credited with the statement “The social responsibility of business is to increase its profits”. The shareholder position on business ethics, as reflected in this statement, is that corporations ought only to pursue shareholder interests. An article from the programme published in the *Journal of Business Ethics*, establishes that this position is ethically untenable. The shareholder position entails strict special duties towards shareholders, which cannot be defended by any reasonable ethical theory. Corporations do in fact have responsibilities to others than their shareholders.

How can we determine what responsibilities corporations have? And do these responsibilities vary with context, for instance between rich and poor countries of operation? These questions can be addressed by applying the so-called assignment approach to corporate responsibility. This approach focuses on the optimal division of moral labour between agents, i.e. an efficient division of moral tasks between corporations, state institutions and other agents. The basic idea is that one can better attain a set of ethical objectives through a delegation of and specialization in specific tasks.

In developed countries a suitable division of moral labour may be for corporations to pursue ownership returns, leaving distributional and other social concerns to the state. However, this division of moral labour breaks down in countries where state institutions are too capacity constrained or dysfunctional to take on their assigned responsibilities. Where other agents (including the state) fail to take on distributional or other social responsibilities, these responsibilities fall on corporations. In other words, for corporations operating in developing countries with a poor institutional setting, responsibilities go beyond maximizing ownership returns.

This line of thinking can also be applied to corporations operating in totalitarian states. From a human rights perspective, there are both

negative duties not to violate rights, and positive duties to create or contribute to systems of rights protection, and to aid those deprived of their rights. The negative duties are universal and must always be respected by corporations. For positive duties, there can be a division of moral labour. Where these duties are borne by public institutions, positive duties of corporations are limited. Where public institutions and others fail to protect rights, these positive duties fall on corporations.

“If a corporation cannot operate without contributing to human rights violations, it should stay out”

The implications for corporations in a country such as Burma are as follows. If a corporation cannot operate without contributing to human rights violations, it should stay out. If a corporation chooses to locate in Burma, it faces demanding positive duties, since rights are disregarded by government and ineffectively advanced by the international community. These positive duties depend on the relative power of the corporation; the more powerful the more extensive the duties. A corporation such as Total Oil in Burma, which is a major player in its oil industry, thus has extensive duties to promote human rights in that country.

ETHICS CAN BE COSTLY, INCENTIVES ARE NEEDED

The claim often made by business executives, that CSR is profitable, is unsubstantiated. Empirical studies on the relationship between CSR and profitability, are inconclusive and largely uninformative due to severe methodological shortcomings. Nor is there a theoretical

justification for the idea that CSR is generally good for profits. The implication is that many of the responsibilities assigned to corporations will not be pursued voluntarily, requiring the imposition of additional incentive mechanisms for firms. The programme has focused on three areas of corporate incentives for CSR; organizational structure, market structure, and executive pay.

“there may be trade-offs between corporate governance reform, and corporate social responsibility”

Executive pay can be fixed or performance-based. A final result established by the programme is that an introduction of performance-based pay decreases effort executives allocate to CSR under certain conditions. This is an important result, which suggests that there may be trade-offs between corporate governance reform, and corporate social responsibility, which is contrary to much of the received wisdom in this area.

“oil company policy on CSR is mainly driven by economic incentives”



DO OIL COMPANIES ACT RESPONSIBLY IN ANGOLA?

The descriptive perspective of the programme, has focused mainly on the conduct of companies in the oil sector in Angola. A survey of oil service firms operating in Angola suggests that, in practice, oil company policy on CSR is mainly driven by economic incentives (it is good for business) rather than by ethical considerations (it is the right thing to do). Consistent with the above normative perspective, the lack of accountable public institutions in Angola, and the central position of oil firms in the Angolan economy, provides a case for demanding greater CSR activities from multinational firms operating in the country.

“norms are formed and reformed through the continued interaction of workers within firms, and interaction between firms”

A code of ethics is unlikely to have a significant and lasting effect on behaviour in an organization where misconduct is sufficiently engrained. An article published in the Journal of Socio-Economics, argues that norms are formed and reformed through the continued interaction of workers within firms, and interaction between firms. By implication, the structure of an organization affects the outcome in terms of norms. Changing widely accepted but unproductive norms may require substantial organizational change. The introduction of a code of ethics must in certain cases be accompanied by an organizational restructuring, to effectively reduce misconduct.

Monopolists are in certain cases less responsible than firms facing perfect competition. This is the result from a model of production plant location in an authoritarian country. On the one hand, there are cost advantages to locating production abroad, on the other, a firm faces consumer reactions reducing demand if the product is produced in the authoritarian country. Surprisingly, for given consumer reactions the cost reductions required for competitive firms to produce abroad are under certain conditions larger than for the monopolist. In other words, monopolists are in certain cases more prone to locate in authoritarian countries than firms facing perfect competition. This result goes against earlier claims in the literature, that monopolists are in a better position to expand CSR activities.



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CONCLUSION

The public debate on CSR is plagued by rhetoric. Corporate executives resort to any excuse to avoid responsibility which cuts into the bottom line. A thousand NGOs make a thousand different demands of corporations. To get from rhetoric to substance, debates and policies need to be informed by ethical theory, which distinguishes between ethically relevant and irrelevant arguments.

The SIP "Business ethics for multinational corporations in developing countries" has grounded corporate responsibility more fundamentally in ethical theory. It has shown that corporate responsibilities go beyond maximizing owner returns, and are more extensive the worse the institutional environment in the country of operation.

Questions of how corporations can most effectively address their responsibilities remain. Moreover, public policy has been dominated by voluntary initiatives such as the EITI or the UN Global Compact. These initiatives are unlikely to take us very far, corporations need to face harder incentives to act on their responsibilities. As the economic models developed under the programme show, getting the incentives right is not necessarily easy. Ethical behaviour can be difficult to elicit, and further work is needed in this area.

Research on corporate responsibility in developing countries will continue at CMI in the years to come, to address these and other question.

FURTHER READING

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